

CEPS COMMENTARY

*Thinking ahead for Europe*

Too cold to handle: EU accession talks with Iceland

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Enlargement has often been hailed as the EU's most effective external policy. Indeed, the transformative power of the pre-accession process has brought remarkable reform and modernisation, especially in the countries of southern, central and eastern Europe. It has helped to expand the zone of peace and prosperity across much of the continent. But the politics of inclusion and harmonisation only work for countries that have a real interest in EU membership. The case of Iceland clearly shows the limits of the Union's power of attraction.

Blowing hot and cold

In its coalition agreement of May 21st, Iceland's new centre-right government decided to freeze accession negotiations with the European Union until Icelanders vote in a referendum on whether they want talks to continue or not. This approach reflects the current eurosceptic mood in Iceland, expressed in the parliamentary elections of April 27th, which inflicted on the pro-EU Social Democratic Alliance (13.5% of the vote) the biggest defeat of any ruling party in the country since independence from Denmark in 1944. The SDA/Left-Green coalition's combined share of the vote fell from over 50% to under 25%. The vote was favourable to the Independence Party (26.5%), which dominated Icelandic politics before 2009, and to the Progressive Party (24.4%), its main rival and partner in the new coalition.

Voters have thus returned the eurosceptic parties that led Iceland to its economic meltdown. While in power, they pushed to privatise the banks and liberalise the financial sector. Iceland's banking-sector assets grew from about 96% of GDP in 2000 to roughly 800% by the end of 2006, and were worth around ten-times its GDP on the eve of the crisis. The Independence Party was in office when Iceland's commercial banks collapsed in 2008 as a result of the global financial crisis, leaving the country with massive debts. The centre-right government collapsed in January 2009 and was replaced in the parliamentary elections of April 2009 by the country's first-ever left-wing coalition government, which had argued that joining the EU would provide long-term economic security for Iceland. It is this government that applied for EU membership on 16 July 2009, in the midst of a banking and economic crisis.

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Formal EU accession negotiations began on 17 June 2010, the day on which EU candidate country status was formally granted by the European Council. Iceland then made steady progress in the accession process. By April 2013, 27 (out of 33) negotiation chapters had been opened; 11 had already been closed. The talks had not yet touched upon the sensitive chapters of energy, agriculture and fisheries, however. The latter, in particular, is something of an emblem for Icelandic voters, who fear that their fishing rights would be eroded by demands from Brussels to grant EU fishing vessels access to Icelandic waters.

As a result of the \$2 billion IMF bail-out package extended to Iceland in 2009 and painful reforms taken to stabilise the economy, the island emerged from recession in late 2011. Many observers saw the country's spectacular recovery as an example for other Western European economies. But Icelanders have not enjoyed the tough love of devaluation, austerity and capital controls over the past four years. Public support for the government has decreased dramatically from 2011 onwards, as evidenced, inter alia, by the negative outcome of two referenda over drafts of a loan agreement proposed after heavy pressure from the Netherlands and the UK. The latter used anti-terrorism legislation against Icelanders to freeze their assets in Britain in an attempt to settle the *Icesave* dispute. Icelandic taxpayers were saved and public opinion was vindicated in a judgment of the EFTA Court of 28 January 2013, which cleared Iceland of all charges. The troubles of the eurozone have also undermined the left-wing parties' pro-EU arguments.

In the run-up to the elections in April, the outgoing government decided to put on hold negotiations over the "difficult" chapters relating to fisheries, agriculture, right of establishment and services and on the free movement of capital, and not to take political decisions related to the EU. However, lower-level, technical discussions continued. After the elections, the European Commission stated that it was prepared to continue with the same dual-track approach unless the new government gave notice otherwise. This has now been ruled out in the new coalition accord, which signals a return to Iceland's conservative political tradition.

Better out than in?

The centre-right parties now say that Iceland would have been worse off as a member of the EU and that devaluation and capital controls have helped to bring recovery sooner than for the eurozone's basket-cases. The Independence Party believes the country's future is best served by staying in the European Free Trade Association (EFTA), of which Iceland has been a member since 1972. EFTA has served as a long-term alternative to EU membership, also for countries like Switzerland, Norway and Liechtenstein, without formally excluding a potential future accession to the EU. Like Norway and Liechtenstein, Iceland is also a member of the European Economic Area (EEA), which was established in 1994 to form a common economic space with EU member states. Moreover, its citizens enjoy the Schengen free movement regime.

As in Norway, the 'loss of sovereignty' argument has dominated public discourse in Iceland. This is astonishing, considering that EU accession would in fact grant Iceland voting status in the Union's decision-making machinery, while within the EEA framework it remains technically obliged to swallow the majority of EU *acquis* without any real participation in its adoption. However, the appeal the EU once held among countries seeking economic stability and access to free trade is diminishing as the Union fails to emerge from its crisis. The UK is openly questioning its allegiance to the EU, while other members, like Denmark, have distanced themselves more clearly from the goal of euro adoption to protect their economies. Iceland now enjoys faster economic growth than the EU average. Eurosceptics ask why Icelanders would want to buy in to and occupy a wing of a building that is on fire.

Recent opinion polls suggest that most Icelanders are indeed against joining the EU. By the same token, however, a majority of those polled are in favour of continuing accession talks.¹ These results and those of earlier polls show that Iceland's relationship with the EU is a deeply divisive issue within the country. Although no date for the referendum has been set, the new centre-right coalition may thus want to settle this matter as soon as possible. Should there indeed be a majority in support of continuing negotiations, then Iceland's accession process will become a complicated and muted affair in the hands of an anti-EU membership coalition government.

Consequences of an Icelandic 'Nei'

Rejection of EU membership would be nothing new. Voters in Norway already delivered this verdict in a nationwide referendum in September 1972. They did so again in November 1994, when they were asked to confirm the EU Accession Treaty that was negotiated and signed in parallel with Sweden, Finland and Austria, which did proceed to membership in 1995. While painful for both the incumbent government and the EU, it has not otherwise hindered the development of EU-Norway relations. Neither has it closed the door to future potential membership of the country. After all, the EU membership clause of Article 49 TEU leaves open the possibility of re-application. Hence Enlargement Commissioner Štefan Füle's recent statement that

“[t]he European Commission continues to be convinced that the EU accession of Iceland would be of mutual benefit and remains committed to accompanying Iceland on its path towards EU membership.”

The current developments in Iceland cast a cool shadow over the EU's parade in welcoming Croatia as the 28th member state on July 1st. Iceland's decision to freeze its accession process may also have a negative impact on Montenegro, which risks losing a valuable advisor in its accession negotiations with the EU. More generally, and contrary to Olli Rehn's prediction that the prosperous and well-integrated North Atlantic country would join the EU together with Croatia in 2011, the sorry state of Iceland's accession process raises the question whether the EU is devoting enough effort to communicating the benefits of enlargement to a generally undecided but increasingly sceptical audience. The *Icesave* dispute highlighted a lack of sensitivity on the part of the EU to what was a very emotional issue for Iceland. Lessons could be drawn here – if and when EU accession negotiations resume.

¹ Survey by the University of Iceland of 23 April 2013 (<http://www.ruv.is/frett/meirihluti-vill-halda-affram-vidraedum>).